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C O N F I D E N T I A L SECTION 01 OF 03 HONG KONG 003794

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DEPARTMENT FOR EAP, EAP/CM  
NSC FOR DENNIS WILDER, KURT TONG

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TAGS: PGOV PREL PINR OVIP ECON CH HK

SUBJECT: VISIT TO HONG KONG OF EAP DAS THOMAS CHRISTENSEN

Classified By: Consul General James B. Cunningham; Reasons 1.4 (b, d)

¶1. (C) Summary: During his September 14-16 visit to Hong Kong, EAP DAS Thomas Christensen reviewed Hong Kong economic and political issues with Financial Secretary Henry Tang, who said the central government leadership in Beijing closely followed but did not fully understand political developments in Hong Kong. Tang also inquired about U.S. Treasury Secretary Paulson's interests in the PRC and addressed the

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need for Hong Kong to implement a goods and services tax (GST). DAS Christensen exchanged views on a wide range of local and regional issues with key political and business leaders. Christensen also discussed economic and political developments in both Hong Kong and the mainland with members of the AmCham Board of Governors and with former Hong Kong Chief Executive Tung Chee-hwa. End Summary.

Financial Secretary Henry Tang

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¶2. (C) On September 15, DAS Christensen called on Financial Secretary Henry Tang, the third-ranking official in the Hong

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Kong Government (HKG). Tang advised that Christensen should "never bet against Hong Kong;" despite the "many challenges" of the past few years, the Hong Kong Special Administrative Region's (HKSAR) economic performance "could not have been much better," with recent GDP growth of nearly eight percent, unemployment at a five-year low, inflation at just two percent, and a government budget surplus.

¶3. (C) Asked about Hong Kong's ability to influence developments in the mainland, Tang referred to U.S. Treasury Secretary Paulson's recent speech regarding active engagement

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and its accompanying responsibilities. Tang said the PRC leadership was conscious of these responsibilities but also looked to Hong Kong for assistance in raising its standards, although there remained many systemic barriers and problems with vested interests. Hong Kong, he believed, could influence developments in the PRC in some ways, but not in a huge way. Tang said the Beijing leadership was aware that the Hong Kong people aspired to directly elect their Chief Executive in 2012 or 2017, but also understood that such a change would lead mainlanders to ask why they could not enjoy the same right. The PRC Government, however, did not understand why a normal citizen in Hong Kong could bring suit against the HKG and possibly win a court judgment. For those sorts of reasons, any changes to Hong Kong's Basic Law required the approval of the National People's Congress

Standing Committee (NPCSC), and Beijing remained "very vigilant" regarding political developments in Hong Kong.

¶14. (C) Again inquiring about Secretary Paulson's speech, Tang asked if Paulson had a "broader agenda" beyond money laundering, exchange rates, economic reform, and the environment. DAS Christensen replied that environmental protection was an issue of personal importance to Secretary Paulson. The issue is also important to the PRC's long-term economic future. Tang replied that it would be beneficial if the Hong Kong people became more interested in environmental issues, as Hong Kong suffered more than any other locality from pollution in Guangdong Province. He acknowledged that the 90,000 Hong Kong-owned factories in the Pearl River Delta region were major contributors to the pollution problem, and that any improvement would require all parties to work together.

¶15. (C) Asked about the HKG's GST proposal, Tang said now was an opportune time for such a measure, despite the "overwhelming" criticism the plan had received. Hong Kong faced an aging population, falling tax revenues, and rising educational expenses that now consumed one-fourth of the government's expenditures. Under these circumstances, Tang believed it was important to increase public understanding of the issue, even if the GST proposal could not succeed at this time. Somewhat similarly, Tang defended the HKG's recent apparent retreat from its "positive non-intervention" economic policy of the 1970s. He said Hong Kong remained essentially a market economy and a capitalist society, and quoted former Financial Secretary Antony Leung's description of the HKG as a "proactive market enabler" in a situation where the "market leads and the government facilitates."

#### Lunch with Political and Business Leaders

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¶16. (C) The Consul General hosted a luncheon for DAS Christensen at his residence on September 15. Present were a selection of Hong Kong's economic, political and journalistic

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elite, representing a range of political stances. DAS Christensen opened the lunch with a short tour of Washington perspectives on the U.S. China relationship and then briefed the gathering on some of the conversations he had had in Beijing. The group generally agreed that U.S.-China relations were at a relatively positive point, as exemplified by China's cooperation with the U.S. in voting for UNSCR 1695 on North Korean missile and WMD programs. Several of the participants noted, however, that the seeming rise of nationalistic reaction against acquisitions of U.S. firms by China- or Middle-Eastern-linked corporations, such as the Unocal and Dubai Ports cases, made Hong Kong and Chinese business people very uneasy. Democratic Party leader and Legco member Martin Lee rejoined, however, that a reduction in China's prosecutions of human rights activists and other abuses would make it easier for people in the U.S. to be more sympathetic to such corporate acquisitions. A discussion ensued about the growing nervousness of the central government as it dealt with rising civil unrest and growing income gaps. Journalist and former Liberal Party chairman Allen Lee remarked that many of his contacts in China are concerned that conservatives are on the rise in Beijing and are attempting to push aside the "Shanghai gang." He does not believe this is coming from Hu Jintao or Wen Jiabao directly, but they feel compelled to accommodate this drive. Daniel Fung, chairman of Hong Kong's Broadcasting Authority and local CPPCC deputy, agreed, saying that there is a broad sense that the reforms of Zhu Rongji and Jiang Zemin went too far, too fast, to the benefit of the coasts and detriment of the hinterland. Businessman, CPPCC delegate and non-official Hong Kong Exco member C.Y. Leung said his mainland government contacts are exceedingly concerned about spontaneous outbursts of public violence, touched off by street arguments or traffic accidents. Crowds have wrecked police cars and

set them ablaze, in a reaction to grinding poverty and frustration.

AmCham Briefing

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¶ 7. (C) In a September 15 meeting with members of the Hong Kong American Chamber of Commerce (AmCham) Board of Governors, one former AmCham chairman emphasized the importance of senior USG officials visiting Hong Kong to hear the views of U.S. and Hong Kong business leaders as well as Hong Kong Government officials, and also to understand political and economic developments here. One member, a former U.S. Consul General, noted the importance of keeping Hong Kong on the US-PRC bilateral agenda, not only for business issues but also for concerns about the rule of law and democratization.

¶ 8. (C) One Board member observed that recently the HKG appeared to be "taking a step backward" by "slamming" former Hong Kong Chief Secretary Anson Chan's possible candidacy for the 2007 Chief Executive election. The member believed the HKG was "not so committed" to the cause of liberal democracy, and that the central government in Beijing both worried about and distrusted the people of Hong Kong. Another member opined that Beijing's "greatest fear" was not Hong Kong independence, but rather that the former colony might descend into a level of "chaos" similar to that they believed prevailed in Taiwan.

¶ 9. (C) Another Board member noted HK's continuing role as an "investment management center" for southern China, with a continuing flow of foreign direct investment through Hong Kong to the mainland. Although there was growing competition between Hong Kong and Shanghai for the role of China's "business center," over the last three years Hong Kong had offered the largest initial public offerings (IPOs) in the world, including some for extremely large PRC companies that were "new" to international business. Hong Kong remained a good place for foreign investors to enter the PRC and also for Chinese companies to enter the world. In general, the AmCham representatives did not view Hong Kong's proposed goods and services tax (GST) as a major obstacle to foreign investors, since introduction of the GST could lead to reductions in other taxes. They believed, however, that the HKG had mishandled the proposal's roll-out and subsequently had been surprised by the public's strongly negative reaction. Further, the Chief Executive's recent remarks about becoming more interventionist in economic management resonated unfavorably in the foreign business community.

¶ 10. (C) In response to one member's observation that US companies could transmit a "tremendously positive" message to the mainland, especially in terms of the potential for an

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individual to rise to the top of an organization, DAS Christensen said the U.S. could work simultaneously at two levels, with both the USG and U.S. foreign investors pushing for democracy. He added that U.S. business leaders in China could remind the PRC leadership that no other country had done more to assist the economic growth of the PRC since 1978, and that a collapse of the PRC was not in the interest of the U.S. or any other western country.

¶ 11. (C) Asked about simmering bilateral disputes between the PRC and Japan, DAS Christensen told the AmCham members that PRC-Japan relations were at a difficult stage due to a volatile mix of historical and nationalistic issues. He said the PRC government tended to "play up" these issues, but nevertheless remained sincerely troubled by Japan's refusal to acknowledge historical events. This trend is not helpful because the PRC would continue to attempt to isolate Japan in the region. Japan needs to improve its relations with South Korea in particular. DAS Christensen said the issue of North Korea remains critical and the USG's pursuit of a

multilateral resolution was absolutely correct, while the "cost of failure" of this effort for the region would be enormous.

¶12. (C) On Taiwan, DAS Christensen told the AmCham governors that ongoing US-PRC tension, in any area, tended to raise PRC concerns about USG military cooperation with Japan and South Korea. Nevertheless, he believed Beijing remained fairly confident that the USG was not promoting Taiwan independence.

Christensen described his recent meeting in Shanghai with Fudan University students, during which he argued that while there were "problems" in Taiwan's democratization process, the Taiwan people remained able to discuss these issues freely. On direct links between Taiwan and the mainland, Christensen said that whoever won Taiwan's 2008 presidential election would be likely to push for expansion of direct links, which the USG supported. Before such conditions are in place, it would be difficult for the United States to consider seriously a U.S.-Taiwan Free Trade Agreement.

Former Chief Executive Tung

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¶13. (C) Former Hong Kong Chief Executive Tung Chee-hwa told DAS Christensen that the Beijing leadership was attempting to address all the key issues on its agenda, including financial reform, North Korea, Taiwan, and relations with the U.S. and Japan. Of these issues, by far the most important for Beijing was Taiwan. Asked about the recent announcement by Beijing of apparently increased restrictions on foreign media operations, Tung noted that the announcement was issued while Premier Wen Jiabao was in London, forcing him to address the issue; Tung said Wen's response suggested that the restrictions could be reversed. Tung was very interested in the visit to the PRC of Treasury Secretary Paulson, at one point asking his assistant if she had obtained a copy of Paulson's speech. Tung also devoted considerable time to discussion of environmental issues in both the mainland and Hong Kong, including the general lack of local enforcement of national laws and regulations in the mainland.

¶14. (U) This message was cleared by DAS Christensen.

Cunningham